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SUBJECT: MOZAMBIQUE: 2005 INVESTMENT CLIMATE STATEMENT

REF: 04 STATE 250356

The following is Embassy Maputo's Mozambique Investment Climate Statement 2005.

Mozambique Investment Climate Statement 2005

Chapters:

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Overview

Mozambique has emerged from its conflict-torn past to become one of the most rapidly growing economies in Sub-Saharan Africa. Mozambique's macroeconomic reforms and success in attracting large investment projects have given the country an average GDP growth rate of eight percent from 1992-2004, the highest in Africa over this time period. In the past, political risk, corruption, bureaucratic red tape, dilapidated infrastructure, and the relatively small size of the market served as strong deterrents to foreign investment. Many of these issues remain concerns for investors, but the investment climate continues to improve. The government's policy of granting management concessions and allowing the privatization of transportation networks is both encouraging more outside participation in the Mozambican economy as well as opening up areas of the interior for investment. The donor community has provided substantial funding to improve the country's infrastructure. In particular, USAID has assisted the government to develop and rehabilitate important roads, bridges, and rail lines. Although Mozambique has attracted several large investments, there is still much room for improvement in streamlining the permit process and creating a more investment-friendly business climate. Small and medium-sized enterprises (SMEs) struggle to start up and operate in the current business environment. The private sector and donors have encouraged the government to begin a process of commercial, financial, and labor reform to address current business and investment obstacles. The government has responded by proposing policies, in coordination with the private sector, that could improve the investment climate significantly over the next several years. There remains significant scope for additional reforms in the mid- and long-term, especially in the implementation of these new policies and laws.

Openness to Foreign Investment

Mozambique encourages foreign direct investment. The CPI, the government's Investment Promotion Center, has been active in bringing investors into Mozambique and should be a potential investor's primary contact with the government. The CPI is particularly interested in increasing investment in the central and northern regions of the country in order to decrease large regional development imbalances.

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Foreign investment in Mozambique is governed by the Law on Investment, No. 3/93 of June 24, 1993. Additional amendments were passed in Decree No. 14/93 on July 21, 1993 and Decree 36/95 on August 8, 1995. The law and amendments generally do not make distinctions based on investor origin, nor limit foreign ownership or control of companies. Lengthy registration procedures can be problematic for any investor -- national or foreign. Working with a local consulting firm or partner familiar with the requirements will facilitate the registration process. The "Doing Business in 2004" report by the World Bank identifies Mozambique as one of the most difficult countries to start a business. Entrepreneurs can expect numerous bureaucratic hurdles that must be overcome sequentially to launch a business. In 2004 the average time to open a business was 153 days, although recent discussions with local businesspeople indicate the whole process might be moving slightly more quickly. The government hopes in 2005 to shorten the period 60 days. Donors are assisting this effort. In general, large investors receive much more support from the government in the business registration process, while small and medium-sized investors endure lengthy, bureaucratic delays. The CPI will assist foreign investors in obtaining licenses and permits. To date Mozambique's privatization program has been relatively transparent, with open and competitive tendering procedures in which both foreign and domestic investors have participated. Most remaining parastatals are in public utilities, making their privatization more politically sensitive. While the Government has indicated an intention to take on partners for most of these entities, progress has been slow. Government authorities must approve all foreign and domestic investment. The CPI handles the approval process for foreign investors. The investment approval process is automatic within 10 days, if no objections are voiced by: 1) the relevant ministries; 2) the provincial governor for investments under \$100,000; or 3) the Minister of Planning and Finance for investments between \$100,000 and \$100 million. The Council of Ministers must review investments over \$100 million and those involving large tracts of land (5,000 hectares for agriculture, 10,000 hectares for livestock or forestry projects). The Council has 17 working days to voice an objection before approval becomes automatic. The government has not used screening mechanisms to limit investment or protect domestic industry.

----- Conversion and Transfer Policies -----

Access to foreign exchange was greatly liberalized by the passage of a new Exchange Control Regulation Law, No. 3/96, promulgated on January 4, 1996. Foreign exchange retention accounts are permitted for 100 percent of foreign exchange earnings, without formal justification. These may be used to purchase imports. Investment registration and repatriation application procedures must be followed to repay foreign loans and for the repatriation of invested capital, profits, and dividends in amounts greater than \$5,000. Application procedures include the presentation of audited accounts and registration through the CPI. A repatriation certificate is then issued from the Central Bank. Debt servicing also requires a letter from the Central Bank indicating bank approval at the time of the loan. Delays are uncommon beyond those typical for administrative processing in a developing country.

----- Expropriation and Compensation -----

Private property was nationalized throughout Mozambique in 1975, following independence from Portuguese colonial rule. After Mozambique's turn away from socialism in the 1980s, citizens had a period of time to reclaim residential property. The government retained commercial property, and later sold it off as part of its privatization efforts. All but a handful of religious properties that were nationalized have been returned; negotiations are ongoing for the rest. There have been no significant cases of nationalization since the adoption of the 1990 Constitution. According to Mozambican law, "When deemed absolutely necessary for weighty reasons of national interest or public health and order, the nationalization or expropriation of goods and rights ...shall (result in the owner being) entitled to just and equitable compensation."

----- Dispute Settlement -----

The current commercial code in Mozambique dates from the colonial Portuguese code of 1888 and does not provide an effective basis for modern commerce or resolution of

commercial disputes. A much-needed reform of the code is in process, but progress has been slow. The judicial system in Mozambique is largely ineffective in resolving commercial disputes. Instead, most disputes among Mozambican parties are either settled privately or not at all. The business community is still so small that a commercial dispute or accusation of illegal activity can seriously damage one's reputation. In February 1999 the National Assembly passed alternative dispute resolution (ADR) legislation. Two ADR facilities, supported by USAID and run by the Center for Commercial Arbitration, Conciliation, and Mediation (CACM) -- one in Maputo and the other in the north in Nampula City -- offer commercial arbitration and are functioning successfully. CACM does not deal directly with labor issues, however. For disputes between international and domestic companies, the law closely follows UNCITRAL, the United Nations Commission of International Trade Law. For domestic arbitration, the law is formulated to cover potentially a wide range of disputes, including non-commercial ones. Mozambique acceded in mid-1998 to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

----- Performance Requirements/Incentives -----

Mozambique generally is in compliance with WTO TRIMS obligations. A variety of tax incentives exist to encourage direct foreign investment, which vary according to the region of the country and the nature of the investment but often include a 50 to 80 percent reduction in industrial and supplemental taxes. Customs exemptions are possible for the importation of capital equipment and raw materials. To qualify, a minimum investment of \$50,000 and pre-approval from the CPI are required. The government grants special fiscal, labor and immigration arrangements to companies operating in designated Rapid Development Zones. Rapid Development Zones include the whole of Niassa Province, Nacala District, Ilha de Mocambique, Ibo Island, and the Zambezi river valley. Investments in these zones are exempt from import duties on certain goods, from real property transfer tax, and are granted an investment tax credit equal to 20% of the total investment (with a right to carry forward for five years). Specific performance requirements are built into mining concessions and management contracts, and sometimes into the sale contracts for privatized entities. Investments involving partnerships with the government usually include milestones that must be met for the investor's project to continue. The process of obtaining visa and related work permits in Mozambique is lengthy and overly bureaucratic. The Ministry of Labor must approve the employment of foreigners. Once the Ministry approves an application, a DIRE (a work permit/identification card), is issued by the Ministry of the Interior (Immigration Department). Assistance through a local lawyer, consulting firm, or an individual familiar with the process will facilitate obtaining a work permit.

----- Right to Private Ownership -----

The legal system recognizes and protects property rights to buildings and movable property. Private ownership of land, however, is not allowed in Mozambique. The government grants land-use concessions for periods of up to 50 years, with options to renew. The government at times has granted overlapping land concessions. Essentially, land use concessions serve as proxies for land titles. Land surveys are being carried out throughout the country to enable individuals to register their land concessions. This process is moving slowly and will not provide any real legal protection to an investor for some time to come. Use of leases as collateral is still not allowed because of lack of adequate land records. The Mozambican banking community uses mortgages on items other than land.

----- Protection of Property Rights -----

The inefficient nature of the Mozambican judicial system makes protection of such rights extremely problematic. Intellectual property right infringement is not a significant problem for US companies due to the small size of the Mozambique market. However, trade in pirated copies of audio, videotapes, DVDs and other goods does occur. The law guarantees the security and legal protection of industrial property rights, copyrights, and other related rights. The National Assembly passed a new copyright and related rights bill in 2000. This bill, combined with the 1999 Industrial Property Act, brought Mozambique into compliance with the WTO Agreement on the Trade Related Aspects of Intellectual Property Rights (TRIPS).

Transparency of the Regulatory System

Regulations governing businesses are antiquated and may be contradictory, and therefore a new commercial code is urgently needed. Bureaucracy associated with all aspects of doing business in Mozambique remains a serious problem. Investors face a myriad of requirements for permits, approvals, and clearances, all of which take a significant amount of time and effort to obtain. Bribes are often requested or offered to facilitate transactions. The government is aware of the problem and has launched a donor-funded effort to streamline procedures across the board. The Ministry of Justice is working to combine proposed government and private sector drafts of a new commercial code. The new code is not likely to reach the National Assembly until 2006.

Regulations in the areas of labor, health and safety, and the environment routinely are not enforced. However civil servants have threatened at times to enforce antiquated regulations that remain on the books to obtain favors or bribes.

Efficient Capital Markets and Portfolio Investment

Mozambique has a small capital market of ten commercial banks. The banks all compete vigorously for clients and deposits. Access to credit for the private sector remains difficult and expensive -- interest rates for loans often fall between 24 and 28 percent per year. Access to capital in the rural areas is constrained by the fact that land leases cannot serve as collateral. Various development agencies, such as the Aga Khan Foundation, offer micro-credit financing programs to fill this need, albeit at high rates. The lack of a rural credit market has inhibited the spread of financial institutions beyond Maputo. Small cities often have one bank, offering prohibitively high interest rates to a captive market. The tiny stock exchange, founded in October 1999, lists shares in one company (a local brewery named Cervejas de Mocambique) and five government bonds.

Political Violence

There were few incidents of localized violence prior to the 2004 general elections. RENAMO supporters complained of intimidation and arbitrary arrests during the December 1-2 voting. In May 2004 many opposition parties and FRELIMO subscribed to an electoral code of conduct, which was generally upheld during the campaign and the elections. Although not legally binding, the code committed the parties to avoiding acts of violence during the campaign and election.

Labor unions are becoming more vocal, but still do not have the financial and institutional capacity to be very effective. Protests rarely turn violent. As in many capital cities, crime is problematic in Maputo. Home assaults, car jacking, and highway robbery are the most prevalent forms of violent crime. Such acts have been on the rise over the past few years, but have not reached the same proportions as in neighboring South Africa.

Corruption

Corruption is a serious problem in Mozambique. Bribe-seeking activity by officials is commonplace. Senior officials often have conflicts of interest between their public roles and their private business interests. Bribery is considered a criminal offense in Mozambique. Political declarations repeatedly have been issued denouncing corrupt practices and promising actions against the guilty. However, such actions have been extremely slow in coming. Investigations rarely result in convictions, unless the accused has relatively minor status in society, while senior officials are seldom, if ever, investigated. The media is unafraid to report on corruption, however. Over the past three years the United States has been the lead donor in providing assistance to the government to fight corruption. With US resources, the government set up an Anti-Corruption Unit in the Office of the Attorney General, charged with investigating and prosecuting corruption-related crimes. The National Assembly passed a new anti-corruption bill in 2004 that updates previous antiquated legislation. Civil society has become more vocal on corruption-related issues, with some support from the US government. One U.S.-supported NGO, Etica Mocambique, is quite active in pressuring the government to act against corrupt practices. Etica runs a civic education campaign to help citizens identify and protect themselves against corrupt officials or activities. Among other achievements Etica has established several corruption reporting centers, which give citizens free legal advice, and a mechanism for discreetly reporting corruption-related crimes to the Attorney General's office.

Mozambique is a signatory to the United Nations Convention Against Corruption.

----- Bilateral Investment Agreements -----

In December 1998 Mozambique negotiated a Bilateral Investment Treaty (BIT) with the US. The U.S. Senate ratified the treaty in November 2000, followed by the Mozambican Council of Ministers in December 2004. The BIT is expected to come into force early in 2005. Mozambique has also signed bilateral investment agreements with South Africa, Portugal, Zimbabwe, Mauritius, France, Italy, China, Egypt, Indonesia, Algeria, Switzerland, Germany, the Netherlands, Sweden, Denmark, the UK and Cuba. South Africa is Mozambique's biggest trading partner and the largest source of foreign investment. Since 1995 Mozambique has engaged in regular discussions with South Africa to harmonize trade regulations and facilitate cross-border trade and investment. Other countries with investment in Mozambique include Portugal, Japan and Great Britain. The United States is a minor trading partner and has modest investments.

----- OPIC and Other Investment Insurance Programs -----

The Overseas Private Investment Corporation (OPIC) has provided financing to two ongoing projects in Mozambique - the privatization of transportation services along the Nacala corridor (port and railway) and tourism development on the coast. Mozambique is a member of the Multilateral Investment Guarantee Agency (MIGA), part of the World Bank Group.

----- Labor -----

The estimated work force is 9.2 million (out of a total population of 18 million). In 2004 the government increased the country's minimum wage by slightly more than the 2003 inflation rate of 13%: the minimum wage for industry, services, and the civil service rose by 14%, from \$41 to \$47 per month; the minimum wage for agricultural works rose by 15%, from \$29 to \$34 per month. Many work several jobs to make ends meet and often grow corn and vegetables on a small plot of land for personal consumption. An estimated 81% of the labor force works in agriculture, 6% in industry, and 13% in services. Nationwide literacy levels are estimated at 47 percent (2002 World Bank figure), with urban centers accounting for the majority of literate adults. Labor unions created during the socialist years of the 1970s and 1980s remain strong and are asserting greater independence from the ruling party, FRELIMO. Total membership among Mozambique's fourteen unions is close to 200,000. A major concern for the unions is the minimum wage. Another important matter for the unions is the privatization and/or restructuring of state-owned enterprises, which often lead to layoffs of union employees. Labor unions are exerting considerable pressure on the government to maintain extremely pro-worker provisions in new labor legislation expected in 2005. Potential investors should be aware that they could incur costly financial liabilities related to severance payments and other benefits. It is essential to obtain reliable legal counsel on labor code requirements.

----- Foreign Trade Zones/Free Trade Zones -----

The government is anxious to see industrial free zones (export processing zones) take hold, and Decree no. 61/99 of September 21, 1999, supports this. These regulations established an Industrial Free Zone Council, which approves companies as industrial free zone enterprises, thereby providing them customs and tax exemptions and benefits. There are two essential requirements for Industrial Free Zone status: job creation for Mozambican nationals and the exportation of at least 85% of annual production. Industrial Free Zone developers enjoy an exemption from customs duties, VAT, and Specific Consumption Tax on the importation of construction materials, machinery, equipment, accessories, accompanying spare parts, and other goods destined for the establishment and operation of the Industrial Free Zone. The processing of cashew nuts, fish, and prawns are not acceptable industrial free zone activities. Free zone concessions are granted for a renewable period of 50 years. Mozambique's big commercial success stories, such as MOZAL and SASOL, operate in industrial free zones.

----- Infrastructure -----

While there has been significant investment in

infrastructure to repair damage of the civil war and the devastating floods of 2000, progress is still somewhat uneven. Many larger cities have relatively well-developed transportation, energy, water, sanitation, and telecommunication systems, while large sections of the country have few or none of these systems in place. This can be a challenge for an investor, especially in rural areas. Some investors should consider that they might need to provide and maintain their own infrastructure (roads, power, water, sewage) with little local help, since no one with required technical skills may be available.

----- Foreign Direct Investment Statistics -----

Foreign Direct Investment -- The government established the Investment Promotion Center (CPI) in 1985. From January 1, 1990 through December 31, 2003 a total of 1,852 projects were approved under the law of investments, creating an estimated 225,835 jobs and totaling USD13 billion in investment. Foreign direct investment accounts for USD 3.3 billion of this amount, USD 872 million represents national direct investment, and the remainder consists of loans, reinvestments, and subsidies. (All statistics cited here are from the CPI.)

Maputo province attracted the largest amount of investment in 1990-2003, totaling USD 2.2 billion. Gaza, Nampula, Sofala, and Zambezia provinces ranked next, at USD 510 million, USD 158 million, USD 116 million, and USD 102 million in investment, respectively. The investments went to the following sectors: industry (USD1.7 billion), minerals and energy resources (USD 631 million), agriculture and agro-industry (USD 260 million), banking and insurance (USD 237 million), and tourism and hotels (USD 209 million).

The CPI supplied the following data on foreign direct investment for projects approved for the 1990 through 2003 period. The breakdown by province is as follows:

Province # Projects FDI USD mil. NDI USD mil. Total

Province	# Projects	FDI USD mil.	NDI USD mil.	Total
Maputo	1,074	2,225	543	8,471
Gaza	80	511	15	1,290
Nampula	124	158	63	515
Sofala	167	116	51	493
Zambezia	86	102	82	482
Inhambane	91	97	13	186
Cabo Delgado	65	58	64	1,232
Manica	70	31	8	125
Tete	62	25	13	180
Niassa	20	1	14	44

Note: Total is the addition of FDI, NDI, and foreign loans.

Projects approved for the 1990 through 2003 period were established in the following sectors:

Sector # Projects FDI USD mil. NDI USD mil. Total

Sector	# Projects	FDI USD mil.	NDI USD mil.	Total
Industry	505	1,658	261	5,025
Mineral/Energy	24	631	21	1,496
Agr/Agro-Proc	353	260	124	1,359
Banking/Insur	40	237	138	409
Tourism/Hotel	182	210	133	1,648
Transport/Com.	185	157	89	1,698
Other	321	87	56	708
Construct/PWrk	131	60	27	491
Aquacul/Fish	111	44	22	278

Note -- The total figure above includes foreign loan amounts, which are not shown.

In 2004 some 143 projects were approved, totaling USD 508 million (this includes FDI, foreign loans, and national private investment). The sectors with the greatest level of investment were: transportation and communications, tourism and the hotel industry, and agriculture and agro-processing. South Africa, Portugal, the United Kingdom, Japan, and Ireland are the top five investors in Mozambique since 1990, and together account for 81 percent of all foreign investment. The U.S. accounts for only 1.4 percent. Mozambique's economy is small enough that one large project still significantly sways investment statistics. Investment statistics from 2004 forward will need to take into account several new, large projects such as the SASOL natural gas pipeline, heavy sands extraction and processing (Moma Heavy Sands Project by Kenmare Resources - Ireland and Corridor Sands by WMC - Australia), and the Moatize mining project (Companhia do Rio Vale Doce - Brazil).

Of the 143 projects approved in 2004, 105 of them involved foreign investment valued at approximately USD 122 million in total. The breakdown of FDI by country of origin is as follows:

Year 2004 Investment

Country # Projects FDI USD Mil.

South Africa	2	59
UK	16	13
India	2	10
Portugal	14	6
Serbia and Montenegro	1	6
Malawi	4	5

Zimbabwe 22 4
Mauritius 2 3
Sweden 3 3
Tanzania 2 2

U.S. investor interest has been growing for several years. In 1996 Seaboard Corporation (Kansas) purchased a state-owned flour mill in Beira through the country's privatization of the state firm, Mobeira. Coca-Cola increased its substantial holdings in bottler SABCO (South Africa Bottling Company) to 24 percent. SABCO has taken over Coke's Maputo bottling plant and has built additional plants in the central region (Chimoio) and the northern region (Nampula) to provide national coverage. Other significant U.S. investors include Mobil Oil, Colgate-Palmolive and a private individual investor working in tourism development in Inhambane province. There is significant (although not majority) US investment in Tenga, Ltd., a macadamia nut plantation in Niassa province. There is also U.S. investment in Indian Ocean Aquaculture (IOA), a shrimp aquaculture project in Cabo Delgado. In early 2005 U.S. firms Railroad Development Corporation (RDC) and Edlow Resources (ERL), majority shareholders in the Nacala Corridor Concession Group, assumed ownership and management of the Nacala port and railway network. This project should bring significant FDI to the transportation sector in 2005.

Foreign direct investment totals in Mozambique from

1990-2004:

Year No. of Projects FDI USD Mil.

1990	31	20
1991	25	21
1992	27	77
1993	29	46
1994	123	136
1995	166	60
1996	270	97
1997	184	558
1998	209	207
1999	235	101
2000	179	230
2001	129	528
2002	128	559
2003	112	122
2004	105	122

Total 1,952 2,884

The following data details total approved foreign direct investment for specific projects in 2004. Data is included for projects that the CPI considers to be in the implementation phase or operational.

Company Sector USD Mil.

Karibu River Estate Tourism 44

CCFB Transportation 10

Transcom Mogambique Telecommunications 10

Marnorte Agriculture & Agro-Industry 5

Proj. Desenvolv. Texteis Industry (Textiles) 4

Mogambique Farms Agriculture & Agro-Industry 2

G.S. Holding Industry 2

Tenga, Ltd. Agriculture & Agro-Industry 2

Indian Ocean Aquaculture Aquaculture & Fishing 2

Companhia de Vanduzi Agriculture & Agro-Industry 2

LA LIME